

CONTRACT NEGOTIATION AS THE KEY TO VENDOR SELECTION

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The paper emphasizes the importance of contract negotiations in making the proper choice of an information system vendor and as a tool to insure a successful system implementation. The topics covered include the negotiating perspective in the planning process, insuring vendor commitments during the evaluation phase, developing a negotiating strategy, preparation for the negotiating session, contract drafting and content.

Rather than relegate contract negotiations to the last-minute reading of fine print, user organizations should seize upon the opportunity to use contract negotiations as a tool for bringing about a successful implementation of an information system. In so doing, the user will at first be cutting across the grain of a long-standing industry practice: the acceptance of unconscionably vendor-protective contracts. The near certain resistance and the added expense of taking the negotiated route will be justified by achieving a positive vendor/user relationship. This relationship should, as a result of good negotiations, be based upon a mutual understanding and a fair allocation of the risks and responsibilities inherent in any transaction involving the transfer and use of complex technology.

In the data processing industry, a clear contractual standard based upon fairness has not yet developed. To the contrary, there is an uncommon devotion to the "vendor's form contract," which nearly always harshly

limits the vendor's responsibility. Moreover, user requirements differ, and thus, a "standard" contract will rarely be appropriate. Contract negotiations should be designed and conducted with the purpose of achieving a fair contract which fits the particular circumstances. After all, the ultimate goal of contract negotiation is to achieve the proper relationship with the right vendor, and the right vendor is the one which can provide, and will agree to be legally bound to provide, exactly what has been promised during the sales cycle. Often, the expectations of the parties are brought into focus for the first time as a result of this process. Thus, contract negotiation is the final step in selecting the right vendor.

Carrying out these complex purposes requires a methodology which is equally complex, but flexible. Based upon their combined experience, the authors believe such a methodology should include early recognition of negotiating perspective in the system planning process; use of communications to achieve voluntary vendor commitments; development and updating of a negotiating strategy and identification of management decision options; planning and conduct of negotiating sessions; and preparation of a comprehensive and accurate contract document.

The Negotiating Perspective and System Planning

Before contacting information system vendors, the user organization should develop a strategic plan which documents the information requirements and relates them to the organization's long-range business plan. The groundwork for successful contract

negotiation is laid during the long-range system planning activity. The more attention paid to development of a negotiating position at this time, the better the user's chance of ultimate negotiating success.

Successful contract negotiation is more than getting the best possible "deal" from a vendor. It requires that at least three constituencies in an organization be satisfied: management, users of the system and those charged with the operation and development of the system. Successful organizations insure that these constituencies, particularly end-users "buy into" the system selection, contract negotiation and system implementation processes by insisting on their participation in the planning and selection processes.

It is important to select the contract negotiation team early in the process, and not later than the conclusion of long-range system planning. Thus, the negotiating perspective will be created prior to the vendor selection phase of system acquisition. Ideally this team should include a member who can speak for the end-users, top management, and for the information systems department. The team should also include legal counsel which specializes in EDP contracting. The team may be augmented by an external consultant, usually the consultant involved in the planning activity.

Use of Communications to Achieve Voluntary Vendor Commitments

After identifying information system requirements, a request for information (RFI) or a request for proposal (RFP) should be prepared. The RFI allows the hospital to screen and eliminate vendors prior to going through the more detailed RFP process. An RFP is more detailed and ordinarily requires a vendor to be very specific about system capabilities and costs. The RFP or RFI can play an important role in contract negotiation. For example, these documents can establish "conditions of bidding" requiring that the vendor's descriptions of system functions and capabilities will become express warranties in the contract. Also, an RFP should require that the vendor's standard form of contract be included in the proposal for review. Other techniques include

structuring the cost section so that the vendor will clearly define what is included in the "price." Vendors should be encouraged to identify additional favorable terms to which they would agree while the competition is active.

While the RFP and proposal are normally the most important of the formal communications between the prospective buyer and the vendor, all written and oral communications are potentially includable in a contract. If the buyer believes the vendor has made a representation or commitment, whether written or not, the buyer should send a letter confirming the vendor's statement.

Development of a Negotiating Strategy and Identification of Management Options

Developing and executing an effective negotiating strategy is unduly and unnecessarily difficult if undertaken after vendor selection has occurred. The psychological exhaustion that occurs after a rigorous vendor evaluation and selection can leave the buyer temporarily defenseless against the vendor that vigorously insists upon its standard contract. Buyers should maximize leverage by planning negotiation before selection. A prime negotiating strategy is to negotiate with more than one vendor simultaneously. This can be the cause of anguish for vendors, unless a positive environment for negotiations has been established. A vendor is naturally concerned that the buyer will use the negotiating process "to play one vendor off against another." The buyer should stress that the buyer is proceeding with contract negotiations to confirm what the vendors have already represented in their proposals, and to incorporate these points and other reasonable provisions into a definitive document. Questions might well be answered in advance by indicating in the RFP that negotiations are part of the vendor selection process. Another challenge in negotiating with two vendors is to gain support from the three user constituencies identified above. These more than the negotiators are often prepared to "settle" with the vendor identified as the first choice. Management especially must become committed to fair contract terms. Well-planned communication within the

user organization is required to obtain this commitment. In the final analysis, however, management's commitment is the key to negotiating success.

Preparation is a paramount strategy for negotiation. The buyer should identify and define problem areas in the vendor offering prior to negotiations. If the product is not well defined, functional specifications should be prepared. If the implementation process is of any complexity, a detailed description of the tasks, responsibilities, and schedules should be developed. An implementation plan, training plan, description of the documentation, and functional specifications should be required components of the vendor's proposals and should ultimately be included or referenced in the final contract. These documents prepared by or with the vendor represent the vendor's voluntary commitment to the service and product desired by the organization. The buying organization's strategy and the additional points to be negotiated tend to be manifested when the buyer requires a proposal structured as described above.

As the negotiating team identifies its strategy, it should be particularly aware of the need to provide for valuable project management options in the contract. EDP contracts almost always contemplate dynamic situations. The parties must anticipate key occurrences during the life of a project and provide for them in the contract. Some of these will relate to actions which should be taken if the system does not pass tests or meet performance expectations. Other options should relate to known uncertainties, contingencies or conditions within the buyer's business environment, such as expansion and contraction of business activity. Still other options are required because of changes and advances in technology. A well constructed, flexible contract will enable the buyer to recover when the vendor fails to perform as expected, will enable the system to be expanded or contracted depending upon the circumstances, and will not rigidly tie the buyer to old technology.

Regardless of the strategy employed, the buyer should insist that the vendor be represented in negotiations by an individual empowered to make

commitments. Valuable time is lost by dealing with others and the vendor gains a negotiating advantage since the vendor can disavow commitment when these are reviewed at higher levels in the vendor's organization.

Conduct of Negotiating Sessions

Assuming that contracting goals and objectives have been identified and prioritized, and the negotiating team has been established, the vendor's voluntary commitments have been documented, and the appropriate contract structure has been identified, the negotiating team should be prepared to conduct effective negotiations. By this point in time the negotiating team should have reviewed all the appropriate documents, including the long-range information systems plan, the RFP, the vendor's proposal, the vendor's standard contract, the system documentation, and the "negotiating position paper." Each member of the negotiating team plays a key role, and each member must understand the role of the other team members. An effective negotiating team rehearses those roles prior to participating in a negotiating session, and it never allows a division among the team members to be visible to the other side. From time to time, the team should update its strategy and re-examine the issues. The contract objectives must be prioritized and reprioritized, to assure that emphasis is placed on overall, major issues. An agenda for negotiating sessions should be established and followed, enforcing the discipline and structure that has been steadily constructed from the last days of long-range planning. Negotiating tactics should be considered, and team members should consult well-known reference works on the strategy and tactics of negotiation.

Contract Drafting and Content

Tradition has suggested that the vendor drafts the initial and subsequent proposed contracts. In addition buyers are tempted to let the vendor control contract drafts in order to conserve effort and cost. The effort and expense of preparing successive contract drafts can be significant, but allowing the vendor to control this activity is false economy. A psychological advantage is gained if it is implied or inferred that only the contract drafter knows enough about the issues to be assigned this task. The organization which controls drafting exercises significant control

over the structure of negotiations. This control extends to the timing of negotiating sessions which can be critical. The non-drafting party may not ultimately save any time or expense since it will be forced to "scrupulously review" each draft to assure that all revisions have been correctly made, no language has been dropped, and no language inappropriately inserted.

Whichever way is chosen, the objective of the contract is to describe as clearly as possible what will be delivered. The intent is to avoid problems which arise from vague or ambiguous statements. The contract is preferably an integrated document for the hardware, software, hardware maintenance and software support. The contract should include a meaningful description of the application packages and associated documentation. Implementation tasks and vendor and user responsibilities should be detailed and scheduled, with emphasis on how, when and by whom these tasks will be completed. Performance of contract obligations by the vendor should be tied to specific dates or times. Objective criteria for judging the satisfactory performance and delivery of contract obligations must be defined. Warranties with respect to the system's functional capabilities and performance on the hardware configuration must be included. Specific provisions for resolution of disputes, temporary relief for reasonable delays and appropriate remedies for nonperformance will provide a framework for overcoming problems during implementation. Counsel experienced in drafting such agreements will be of invaluable assistance to the negotiating team in this regard.

Conclusion

The negotiation process may require several weeks to several months. While the time and effort necessary to achieve a fair contract can be considerable, a contract which is fair to both vendor and buyer is achievable if the parties are committed to that outcome. If so, a practical contract forming the basis of a good relationship between vendor and buyer should result. This is a critical step in achieving a successful implementation of an information system.